

REPORT OF THE AUDITOR-GENERAL TO THE EASTERN CAPE PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE TSOLWANA LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Tsolwana Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets, cash flow statement and the statement of comparison of budget and actual amounts for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2012 (Act No. 5 of 2012) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the *General Notice* issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Unqualified opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Tsolwana Local Municipality as at 30 June 2013, and its financial performance and cash flows for the year then ended in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

7. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

8. As disclosed in notes 35 and 36 to the financial statements, the corresponding figures have been restated as a result of errors only corrected during the year ended 30 June 2013 that existed in the financial statements at, and for the year ended, 30 June 2012.

Material losses

9. As disclosed in note 43.4 to the financial statements, the municipality suffered significant water and electricity losses of 509 795 kilolitres (65,43%) and 4 385 451 kilowatts (45,68%) at a value of R412 934 and R1,80 million, respectively.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

10. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

11. The annual performance report was not presented for audit and consequently my findings below are limited to the procedures performed on the strategic planning and performance management documents.
12. The information was assessed to determine whether performance indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury *Framework for managing programme performance information* (FMPPI).
13. The material findings are as follows:

Usefulness of information

Measurability

Performance targets not specific, measurable and time bound

14. The FMPPI requires that performance targets be specific in clearly identifying the nature and required level of performance, measurable and the time period or deadline for delivery be specified. All of the targets relevant to all key priorities of the municipality were not specific in clearly identifying the nature and the required level of performance, the required performance could not be measured for all key priorities of the municipality and all of the targets relevant to key priorities of the municipality were not time bound. This was due to the fact that management did not consider the evidential and reporting requirements during the annual strategic planning process and, although management was aware of the requirements of the FMPPI, they did not receive the necessary training to enable application of the principles.

Performance indicators not well defined and verifiable

15. The FMPPI requires that indicators should have clear unambiguous data definitions so that data is collected consistently and is easy to understand and use and that it must be possible to validate the processes and systems that produce the indicator. All of the indicators relevant to key priorities were not well defined in that clear, unambiguous data definitions were not available to allow for data to be collected consistently and a total of 58% of the indicators relevant to key priorities were not verifiable in that valid processes and systems that produce the information on actual performance did not exist. This was due to the fact that management did not consider the evidential and reporting requirements during the annual strategic planning process and, although management was aware of the requirements of the FMPPI, they did not receive the necessary training to enable application of the principles.

Compliance with laws and regulations

16. I performed procedures to obtain evidence that the entity has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA, are as follows:

Strategic planning and performance management

17. The municipality did not have and maintain effective, efficient and transparent systems of financial and risk management and internal controls, as required by section 62(1)(c)(i) of the MFMA.
18. The municipality did not set measurable performance targets for the financial year with regard to each of the development priorities and objectives and key performance indicators set out in the integrated development plan (IDP), as required by section 41(1)(b) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and regulations 12(1) and 12(2)(e) of the Municipal Planning and Performance Management Regulation published under *Government Notice R796* in *Government Gazette 22605* dated 24 August 2001 (MPPMR).

Annual financial statements

19. The financial statements submitted for auditing were not prepared, in all material respects, in accordance with the requirements of section 122 of the MFMA. Material misstatements of current liabilities, non-current assets, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

Budgets

20. Expenditure was incurred in excess of the limits of the amounts provided for in the budget and treasury office and corporate services votes of the approved budget, in contravention of section 15 of the MFMA.
21. Quarterly reports were not submitted to the council on the financial state of affairs of the municipality within 30 days after the end of each quarter, as required by section 52(d) of the MFMA.

Audit committee

22. The audit committee did not review the municipality's performance management system or make recommendations to the council, as required by regulation 14(4)(a)(ii) of the MPPMR.
23. The audit committee did not submit, at least twice during the financial year, an audit report on the review of the performance management system to the council, as required by regulation 14(4)(a)(iii) of the MPPMR.

Internal audit unit

24. The internal audit unit did not:
- audit the results of performance measurements, as required by section 45(1)(a) of the MSA and regulation 14(1)(a) of the MPPMR
 - audit the performance measurements on a continuous basis and submit quarterly reports on their audits to the municipal manager and the performance audit committee, as required by regulation 14(1)(c) of the MPPMR.

Human resource management

25. The chief financial officer, the technical services manager and two finance officials at middle management did not meet the prescribed minimum competency requirements on financial and performance reporting, legislation and policy implementation and auditing and assurance, as required by regulations 4, 5, 6, 7, 8 and 9 of the Municipal Regulations on Minimum Competency Levels (MRMCL) published in *Government Gazette* 29967 dated 15 June 2007.
26. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury as required by regulation 14(2)(a) of the MRMCL.

Expenditure management

27. The accounting officer did not take effective steps to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Procurement and contract management

28. Contracts were modified without tabling the reasons for the proposed amendment in the council of the municipality, as required by section 116(3) of the MFMA.
29. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the CIDB Act, 2000 (Act No. 38 of 2000) and CIDB regulation 18.

Consequence management

30. Unauthorised, irregular as well as fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person was liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.

Internal control

31. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

32. There was a lack of oversight and accountability by senior management. Sufficient monitoring controls were not in place to ensure the proper functioning of the overall process of planning, budgeting, implementation, reporting and adherence to internal policies and procedures and compliance with laws and regulations for the purpose of taking corrective action.
33. There was ineffective human resource management resulting in vacant positions that were not filled timeously; officials did not comply with the minimum competency levels, prescribed for financial and supply chain management competency areas. In addition, a performance management system was not in place for all staff.
34. Failed execution of internal control objectives, processes and responsibilities has resulted in unauthorised, irregular as well as fruitless and wasteful expenditure not being prevented and detected.

Financial and performance management

35. The municipality did not prepare reliable, complete and accurate monthly and quarterly financial and performance reports, resulting in material adjustments to the financial statements submitted.
36. The municipality did not have systems in place to monitor compliance with all applicable legislation. Non-compliance with laws and regulations could have been prevented had compliance been properly reviewed and monitored. There was a lack of supervision, monitoring and consequence management in respect of the reporting process.
37. The municipality did not have formally documented and approved user access management and program change management processes for the information technology (IT) system. In addition, outdated anti-virus software is in use. Regular backups were performed, however, these backups were not verified and checked for successful completion and not stored in a secure offsite storage facility. The risk of fraudulent activities and the possibility of losing data increased as a result of the lack of controls of the IT system.

Governance

38. The audit committee was not given sufficient time to discharge its function of reviewing the accuracy, reliability and adequacy of the financial statements and, as a result, the review performed on the annual financial statements did not have the desired impact on the fair presentation thereof as material adjustments, identified during the audit process, had to be made to the submitted financial statements.
39. Although the Municipal Public Accounts Committee (MPAC) was in place during the financial year under review, the responsibilities of the committee were not sufficiently discharged because it only had three meetings during the year under review and sufficient audit evidence could not be obtained to substantiate that MPAC submitted the required quarterly reports to council. Due to this the desired impact of this committee was not experienced.

OTHER REPORTS

Investigations

40. An investigation was conducted into a suspected fraudulent transaction regarding a stolen council cheque. At year-end, the investigation was still ongoing.
41. The investigation conducted into allegations against the former technical services manager, in respect of suspected fraudulent procurement practices, was finalised and the employment contract of the applicable manager was terminated.

Auditor-General

East London

29 November 2013



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence